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TESTIMONY OF CHRISTINE A. BRUENN

President
North American Securities Administrators Association, Inc.
And
Maine Securities Administrator

Before the
Committee on Banking, Housing and Urban Affairs
United States Senate

"Wall Street Analyst Conflicts of Interest Global Settlement"

May 7, 2003

SUMMARY OF NASAA'S TESTIMONY

- The securities administrators in your states are responsible for the licensing of firms and investment professionals, the registration of some securities offerings, branch office sales practice audits, investor education and, most importantly, the enforcement of state securities laws. Some of my colleagues are appointed by their Governors or Secretaries of State, others are career state government employees. Notably, only five come under the jurisdiction of their states' Attorneys General. We have been called the "local cops on the securities beat," and I believe that is an accurate characterization.

- Securities regulatory offices are located in all 50 states and the District of Columbia, and Puerto Rico. We respond to investors who typically call us first with complaints, or request information about securities firms or individuals. Because they are closest to the investing public, state securities regulators are often first to identify new investment scams and to bring enforcement actions to halt and remedy a wide variety of investment related violations. They also work closely with criminal prosecutors at the federal, state and local levels to punish those who violate our securities laws.

- From the outset of the investigations, state securities regulators have had three goals: To fundamentally change the way business is done on Wall Street, by putting investors, not investment banking, first; impose meaningful penalties for illegal behavior; and to provide harmed investors with the information they need to pursue arbitration cases and legal actions against their brokerage firms.

- If the industry follows both the letter and spirit of this agreement, it has the potential to change the culture on Wall Street. Investors – not investment banking fees – will come first. And analysts will be beholden to the truth, not the IPO business.

- While the global settlement is most important for its impact on Wall Street and investors, it is remarkable for another reason as well– it represents a model for state-federal cooperation that will serve the best interests of investors nationwide.

- Investors were harmed by unwarranted and exaggerated research reports. The research reports resulted in a "fraud on the market" in that they caused specific stocks and stocks in the affected sectors to rise out of proportion to their true value. Investors who purchased the specific securities or securities in those sectors experienced losses when the market crashed. Investors purchased through the nine firms named, discount firms, other firms who purchased the research, and online. For these reasons identifying the investors for restitution is very difficult.

- Some of investor losses were due to the inflated research reports, but not all of their losses. It's difficult to determine how much of investor losses are attributable to the exaggerated and unwarranted research reports and how much was due to other market factors.

- The analyst conflicts of interest settlements requires six of the firms to contribute a total of $27.5 million over the next five years for investor education on the state level. The NASAA Board of Directors determined these payments will be directed to the Investor Protection Trust (IPT).

Chairman Shelby, Ranking Member Sarbanes and Members of the Committee,

I'm Christine Bruenn, Maine's Securities Administrator and President of the North American Securities Administrators Association, Inc. (NASAA).[1] I commend you for holding this timely hearing, and thank you for the opportunity to appear before your Committee to present the states' views on the global settlement with ten Wall Street firms.

I would like to start by acknowledging the role that this Committee and its House counterpart played in this matter. Congressional hearings shined an early light on Wall Street practices that were an important guide for regulators.

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Overview

Let me give you a brief overview of state securities regulation, which actually predates the creation of the SEC and the NASD by almost two decades. The securities administrator in your states are responsible for the licensing of firms and investment professionals, the registration of some securities offerings, branch office sales practice audits, investor education and, most importantly, the enforcement of state securities laws. Some of my colleagues are appointed by their Governors or Secretaries of State, others are career state government employees. Notably, only five come under the jurisdiction of their states' Attorneys General. We have been called the "local cops on the securities beat," and I believe that is an accurate characterization.

Securities regulatory offices are located in all 50 states and the District of Columbia, and Puerto Rico. We respond to investors who typically call us first with complaints, or request information about securities firms or individuals. State securities regulators work on the front lines, investigating potentially fraudulent activity and alerting the public to problems. Because they are closest to the investing public, state securities regulators are often first to identify new investment scams and to bring enforcement actions to halt and remedy a wide variety

[1] The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc., was founded in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico and Puerto Rico. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

of investment related violations. They also work closely with criminal prosecutors at the federal, state and local levels to punish those who violate our securities laws.

The role of state securities regulators has become increasingly important as Americans rely on the securities markets to prepare for their financial futures. Today, we are indeed a "nation of investors." Over half of all American households are now investing in the securities markets.

Investigation and Settlement Process

The investigation of the Wall Street firms was a massive undertaking and involved the coordination of 35 states. These states provided the staff and resources to analyze and review millions of documents, depose and interview witnesses, and draft nine comprehensive settlement orders, all in coordination with their federal counterparts.

While the global settlement is most important for its impact on Wall Street and investors, it is remarkable for another reason as well– I believe it represents a model for state-federal cooperation that will serve the best interests of investors nationwide. As they did with penny stock fraud, microcap fraud, day trading and other areas,[2] the states helped to spotlight a problem and worked with national regulators on market-wide solutions. It bears repeating: the states historically and in the current cases, investigate and bring enforcement actions – they do not engage in rulemaking for the national markets. That is rightly the purview of the SEC and the SROs.

None of the regulators who were involved in this global settlement could have done this on its own. Even with the funding increase Congress allocated for the SEC, the Commission can't go it alone. That is why there must be cooperation and division of labor among state, industry and federal regulators.

Over the last several years, NASAA members have been active participants in the rulemaking and legislative process in the area of analysts' conflicts of interest. The states worked closely with the SEC and the SROs both to leverage limited investigative resources and to formulate new, market-wide rules that were needed to fix this problem. In 2001, we commented on the NASD's original rulemaking regarding analysts' communications to the public. We followed that with a letter to Chairman Richard Baker during his subcommittee's public hearing process regarding analysts' practices.

In addition, we commented on the NASD/NYSE's proposed rules relating to research analysts. We complimented the NASD and NYSE on their work, offered general support and made suggestions that we felt could make the rule stronger in some areas. Many of our original proposals were incorporated in the final rule. Also, NASAA was strongly supportive of Title V in S. 2673 which became the Sarbanes-Oxley Act of 2002.

Last spring, as the New York Attorney General was wrapping up its Merrill Lynch investigation, NASAA suggested to Attorney General Spitzer that it would be beneficial to all concerned to settle the case simultaneously for all the states as a group. He agreed, and negotiated on those terms. The case was concluded with all 50 states and the District of Columbia and Puerto Rico joining in the settlement.[3]

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[2] See State/Federal Dynamic Chart Attached
[3] See NASAA Analyst Investigations Chronology Attached

In late April, a few weeks before the Merrill Lynch agreement, the NASAA Board of Directors met to form the NASAA Analysts Task Force. Its Steering Committee was charged with investigating whether problems discovered at Merrill Lynch were industry wide. The Steering Committee assigned one state to lead the investigation of each firm; many other states signed on to assist in the investigations. Further, the Task Force agreed to work collaboratively on the analyst investigation with the SEC, the NYSE and the NASD.

The state investigations continued into November, at which time, in conjunction with the SEC, NYSE and the NASD a determination was made to pursue the resolution of the cases in a global manner. Each firm investigation included a lead state and a federal counterpart. Last December, an agreement in principle was reached with 11 firms; it took intensive negotiations with the firms to reach the final global settlement announced last week.[4]

The Deutsche Bank investigation was not included in the global settlement because the California Department of Corporations discovered the failure of Deustche Bank to produce documents as requested by the Department during its analyst investigation. The reasons for Deutsche Bank's failure to produce documents and whether Deutsche Bank has, in fact, produced all requested documents at this time remains under investigation by the Department (and other state securities regulators such as the District of Columbia and Maryland) in conjunction with the SEC.

Penalties/Restitution

The $487.5 million in penalty monies to the states includes the prior settlement between Merrill Lynch and state securities regulators. Attached to this testimony is a state-by-state chart that lists the distribution of the global settlement penalties based on a population formula with a minimum allocation of one percent of the total.[5] An important question is how best to use that money?

A primary and routine objective of state securities regulators is to obtain restitution for investors as part of enforcement actions. For example, in FY 2002, restitution ordered through administrative or civil actions was $309 million. At the same time, roughly $71 million was ordered in fines and penalties.

In a recent case involving the illegal sale of unregistered products, the Arizona Corporation Commission ordered the defendants to pay over $16 million in restitution to investors. It also assessed administrative penalties in the amount of $133,100. In another case announced last week by the Alabama Securities Commission, the former President of Fabtec Inc. pled guilty to two counts of fraud in connection with the sale of securities and two counts of theft of property in the first degree. A sentencing hearing is scheduled for June. The former president faces up to 60 years imprisonment and the state is seeking restitution in the amount of $1,690,000.

Throughout the eighteen months of the analysts' investigations, state securities regulators wrestled with how best to compensate investors injured by the wrongdoing. Restitution is a viable remedy where victims can be readily identified, where the fraud is direct and person-to-person and where damages are subject to straightforward calculation. In order to satisfy the expectations of the victims, there also needs to be enough money to distribute through restitution so that the recipients receive a sum that represents a meaningful portion of their losses. Unfortunately, we do not believe the analyst cases readily lend themselves to restitution.

[4] See Chart of Investigated Firms and State/Federal Partnership Attached
[5] See Analysts Conflicts Settlements Chart Attached

One of the reasons we have struggled is because it is very difficult to identify the victims of any fraud on the market. We could start with the customers who purchased the stocks through the firms, but what about those who saw Henry Blodget on CNBC and then purchased the stocks online or bought stocks from a firm that purchased research from one of the ten firms? And what about mutual fund shareholders? In our view, in a fraud on the market, *all* investors are harmed. If restitution is available to all investors, it would be an insignificant amount of their losses. If restitution is available to only a subset of investors, it is arbitrary and unfair. In light of these problems, we believe decisions regarding the funds are best made at the state level so they can be tailored to the unique circumstances of each state.

These monies will be allocated according to the governing law in each jurisdiction. For example, in North Carolina, it will go to an investor education fund; in Mississippi, new investigators will be hired for future enforcement efforts; in my state of Maine and in Maryland, the money will go into the general fund and be used for state legislative priorities such as education, prescription drugs and other state provided services.
We expect the combination of monetary penalties, injunctive provisions and the release of evidence that can be used in private actions will deter similar conduct in the future.

Investor Education Funds

The final component of the analyst conflicts of interest settlements requires six of the firms to contribute a total of $27.5 million over the next five years for investor education on the state level. The NASAA Board of Directors determined these payments will be directed to the Investor Protection Trust (IPT).

The IPT is a Wisconsin charitable trust, classified by the IRS as a public charity. The IPT was created ten years ago with $2 million as part of a multistate securities settlement. The Trust's primary focus in recent years has been Financial Literacy 2010 (FL2010), a program designed to increase the amount and quality of personal finance classroom instruction in America's high schools. This initiative gives teachers across America the tools they need to introduce a personal finance curriculum in the high schools. Money from the Trust has been used to provide customized teaching guides and to train thousands of teachers on how to use the guides in their classrooms. FL2010 has also reached teachers through direct mail, exhibits, a quarterly newsletter, and a website (www.fl2010.org).

In addition to FL2010, the Trust has undertaken an extensive investor education mission, including public service announcements, distribution of educational videos on investor preparedness and investment fraud awareness, the Investing Online Resource Center (www.onlineinvesting.org), an independent, non-commercial website dedicated to serving the individual consumer who invests online or is considering doing so, and a non-commercial investor education website (www.investorprotection.org).

The payments from the analyst conflicts of interest settlement will be maintained in a separate, designated fund of the IPT, the Investor Education Fund (the Fund). The Fund will be distributed pursuant to a grant process and used to support and create financial literacy programs and materials tailored to the needs of local communities and to conduct research. The goal of the Trust is to equip investors with the knowledge and skills necessary to make informed investment decisions and to increase personal financial literacy. No principal or income from the Fund shall inure to the general fund or treasury of any State. The Fund will be held in a subaccount, with provisions for fund accounting, annual audited financial statements, and regular reporting on items such as grant applications, expenses and fees incurred.

Ongoing Enforcement Initiatives

The analyst conflict of interest case was a big story in the financial press over the past year. But it was hardly the only focus of state securities regulators. As always, state securities regulators continue to vigorously pursue sales practice abuses and a variety of scams and frauds against unsuspecting investors. There are many types of violations that state securities regulators continue to fight. NASAA has published a list of the "Top 10 Investment Scams" the past several years to highlight problem areas for investors.[6] I'll mention just a few of our ongoing initiatives.

Unregistered Securities - We are continuing to address, in cooperation with the National Association of Insurance Commissioners (NAIC), the chronic problem of insurance agents selling unregistered and fraudulent securities. In hundreds of cases, scam artists are using high commissions to entice insurance agents into selling investments they may know little about to investors for whom they are unsuitable.

On April 17, the Indiana Secretary of State announced the sentencing of a convicted Securities Act violator to 42 years in prison and $110,931 in restitution. This conviction was the culmination of an investigation initiated by the Secretary's office regarding a firm that operated to sell unlicensed securities. The Secretary of State referred the case to the County Prosecuting Attorney to file the criminal charges. These offices worked together to utilize their specialized resources and expertise to sentence a violator to jail.

Examples Unregistered Products

Viatical Settlements – In the wake of a 1996 decision holding that interests in certain viatical settlement policies sold were not "securities" under federal law, there has been a proliferation of these viatical investments sold to investors nationwide in violation of state securities laws. A viatical settlement contract allows an investor to purchase an interest in the life insurance of a terminally ill person.

Almost all state securities regulators take the position that viatical investments are "securities" under their respective laws. Last fall, the NASAA membership approved guidelines for states to adopt that apply to the offer and sale of viatical investments. Meaningful regulation is essential to ensure that neither the lawful viators nor investors are defrauded.

Many states have vigorously pursued enforcement actions due to occurrences of deceptive marketing practices and numerous instances of fraud.

Recently, the Arizona Corporation Commission revoked the registration of a Tucson securities salesman, assessed a penalty of $66,000 and ordered him to repay six investors over $430,000 plus interest in a case dealing with unregistered viatical contracts.

Charitable Gift Annuities - In February 2003, the Securities Administrator issued a Cease and Desist Order against a Tennessee-based company, the New Life Corporation of America, and a Maine insurance agent. The company had offered charitable gift annuities (CGAs) in Maine through an agent and other unlicensed financial professionals who expected to receive at least a 6% commission. (Such commission-based sales of CGAs are rare and disfavored by most charities.) Solicitations for these CGAs allegedly misrepresented that they were

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[6] See "Top 10" Investment Scams Listed by State Securities Regulators Attached

guaranteed, no-risk investments. The action prevented consummation of pending sales to Maine consumers, one of whom, a very elderly man, was about to part with over $1 million.

Local Enforcement

The states also continue to play an important enforcement role with respect to the conduct of licensed broker-dealers and their registered representatives. State securities regulators are often the first place that investors turn when they feel they have not been treated fairly by a broker. One reason for this is our proximity to everyday investors. Each NASAA member has one or more offices within their state, with contact information readily available on the web. Many investors understandably feel that the logical place to start with a grievance is their local state securities regulator.

And our members are quick to respond, even to individual complaints that may not signal the type of widespread abuse of interest to our fellow regulators at the federal and SRO levels. Often, our members will reach out to the firm with an informal inquiry, leading to quick resolution of the investor's concerns without the need for an enforcement action. In other cases, a "for cause" examination prompted by the customer complaint will reveal systemic problems that must be dealt with through more formal enforcement proceedings. These exams complement the routine broker-dealer exams that a significant number of our members conduct.

Closing

Mr. Chairman and members of this Committee, in closing, I would like to offer you my personal opinion based on 18 years as a securities regulator. I believe that now is the time to strengthen, not weaken our unique complementary regulatory system of state, industry and federal regulation. Eighty-five million investors – many of them wary and cynical expect us to remain vigilant, to stay the course – to make sure, that Wall Street puts investors first. We can not and we will not let these millions of investors down.
I pledge the support of the NASAA membership to work with you and your Committee to provide you with any additional information or assistance you may need. Thank you for the opportunity to testify and I look forward to continuing NASAA's excellent working relationship with this Committee.

STATE/FEDERAL DYNAMIC:
HOW STATE DETECTION OF INVESTOR PROTECTION ISSUES LEADS TO NATIONAL RESPONSE

Issues Identified by State Securities Regulators	Problem	National Response
1989 - States determined Penny Stock offerings by newly formed shell companies to be per se fraudulent.[1] These "blank check" companies had no business plan except a future merger with an unidentified company.	**$2 billion/yr. Losses in Penny Stocks**[2]	1990 - Congress passed Penny Stock Reform Act which mandated SEC to adopt special rules governing sale of Penny Stocks (<$5.00 per share) and public offerings of of shares in Blank Check companies (SEC Rule 419).[3]
1991 - States found that rollups of poorly performing public limited partnerships disadvantaged individual investors by not providing meaningful dissenters' rights.	**Lack of dissenters' rights**	1993 - Congress passed the Limited Partnership Rollup Act which mandated that NASD adopt rules containing specific provisions to protect dissenters' rights.[4]
1996-97 - 33 States participated in sweep of 15 broker-dealer firms that specialized in aggressively retailing low-priced securities to individual investors. States found massive fraud in firms' manipulation of shares of start- up companies, most of which had no operating history.	**$6 billion/yr. Losses in Micro-cap Stocks**[5]	1997-98 - Congress held hearings on fraud in the micro- cap securities markets (shares selling between $5-10). 2002 - Congress passed Sarbanes-Oxley Act which made certain state actions a basis for federal statutory disqualification from the securities industry.[6]

[1] *Resolution of the North American Securities Administrators Association Declaring Blank Check Blind Pool Offerings to be Fraudulent Practices* (4 April 1989), NASAA Reports (CCH) ¶7028.

[2] *NASAA Investor Alert*: Penny Stock Fraud (December 1989).

[3] 15 U.S.C. §78o(g); 15 U.S.C. §77g(b)(1).

[4] 15 U.S.C. §78o(b)(12) and (13).

[5] Opening Statement of Senator Susan Collins, Chair, Senate Permanent Subcommittee on Investigations (22 September 1997).

[6] U.S. Senate Permanent Subcommittee on Investigations (22 September 1997 and 10 February 1998); 15 U.S.C. §78o(b)(4)(H); 15 U.S.C. §80b-3(e).

1996-97 - States were the first regulators anywhere to issue uniform interpretative guidance on use of Internet for legitimate securities offerings and dissemination of product information by licensed financial services professionals.[7]	**Risks of Securities offerings on The Internet**	1998 - SEC issued interpretative guidance based on the States' Model on the use of Internet for securities offerings and dissemination of services and product information by licensed financial services professionals.[8]
1999 - In a report on trading of securities on the Internet, States found that investors did not appreciate certain risks, including buying on margin and submitting market orders.[9]	**Risks of Online Trading**	2001 - SEC approved a new NASD rule requiring brokers to provide individual investors with a written disclosure statement on the risks of buying securities on margin.[10]
1999 - In a first-ever report on individuals engaged in day trading, States found that day trading firms failed to tell prospective investors that 70% of day traders would lose their investment while the firm earned large trading commissions.[11]	**Risks of Day Trading**	2000 - SEC approved new NASD rules making day trading firms give written risk disclosure to individual investors. [12] 2001 - SEC approved new NASD and NYSE rules governing margin extended to day traders.[13]

[7] *Resolution of the North American Securities Administrators Association Regarding Securities Offering on the Internet* (7 January 1996), NASAA Reports (CCH) ¶7040; *Resolution of the North American Securities Administrators Association Regarding Internet Advertising of Information on Products and Services* (27 April 1997), NASAA Reports (CCH) ¶2191.

[8] *Statement of the Commission Regarding use of Internet Websites to Offer Securities, Solicit Securities Transactions, or Advertise Investment Services Offshore,* U.S. Securities and Exchange Commission, Release No. 33-7516 (23 March 1998).

[9] *From Wall Street to Web Street: A Report on the Problems and Promise of the Online Brokerage Industry*, Office of the New York Attorney General (22 November 1999).

[10] *Delivery Requirement of a Margin Disclosure Document to Non-Institutional Customers*, U.S. Securities and Exchange Commission, Release No. 34-44223 (26 April 2001).

[11] *Report of the NASAA Project Group on Day Trading*, North American Securities Administrators Association (August 1999).

[12] NASD Rules 2360 and 2361.

NASAA Analyst Investigations Chronology

Date	Event
7/2001	NY Attorney General starts probe into Merrill Lynch.
8/15/2001	NASAA files letter with the NASD in response to the NASD's request for comment on proposed changes to NASD rules governing analysts communication with public.
4/12/2002*	Attorney General Spitzer sends subpoenas to 12 investment banks with significant research and investment banking revenues requesting that they supply documents that will address analyst's roles in investment banking. (*Not all subpoenas sent out on same date).
4/18/2002	NASAA files letter with SEC in response to SROs' proposed rules addressing analyst conflicts of interest. NASAA suggests that while the rules are a good start, they need to be more expansive.
4/18/2002	NASAA Board of Directors meets to form NASAA Analysts Task Force to be charged with investigating whether problems discovered at Merrill Lynch are industry wide.
4/25/2002	NASAA/SEC/NASD/NYSE agree to work collaboratively on analyst investigation.
4/26/2002	NASAA Analyst Task Force assigns a lead state to investigate each target firm identified by the NYAG in its subpoenas and asks other states to volunteer to assist in the investigation under the management of the lead state.
5/14/2002	NASAA Board approves $2.5 million budget for analyst investigation.
5/21/2002	NYAG settles with ML to agree to terms of settlement. Settlement contains proposed settlement provisions with other states.
6/18/2002	NASAA Board endorses sending settlements to all the states.
6/20/2002	NASAA sends states template to be used in ML settlement.
9/20/2002	NASAA signs contract with Case Central, an electronic discovery company, to assist the states in search, organizing and sharing discovery documents.

9/24/2002	NASAA files letter with SEC in response to proposed rule for Analyst Certification.
10/03/2002	NASAA/SEC/NYAG/NASD/NYSE agree to work together in an attempt to conclude the investigations in a speedy fashion.
12/20/2002	Tentative settlement agreement reached among almost all target firms among states, SEC, NASD, NYSE for $1.4 billion in fines and other payments.
03/10/2003	NASAA submits comment letter to SEC in response to SROs' amendments to rules filed in 2002 noting that the SROs for picked up most of NASAA's suggestions from its 4/18/2002 letter.
4/28/2003	Reach final agreement among almost all target firms, lead states, SEC, NYSE and NASD.
5/1/2003	Draft settlement documents distributed to non-lead states for execution.

ANALYST CONFLICTS OF INTEREST TASK FORCE INVESTIGATORS

FIRM	LEAD STATE	OTHER PARTICIPATING STATES	FEDERAL REGULATOR
Bear Stearns	New Jersey	Delaware, Hawaii, Maine, Pennsylvania, and Vermont.	NYSE
Credit Suisse First Boston	Massachusetts	Virginia	NASD
Goldman Sachs	Utah	Kansas	NYSE
J.P. Morgan Chase	Texas	Arkansas, Idaho, Missouri,	NYSE
Lehman Brothers	Alabama	Georgia, Indiana, Mississippi	SEC
Morgan Stanley	New York		SEC
Piper Jaffray	Washington	Iowa, Minnesota, and Wisconsin	NASD
Salomon Smith Barney	New York	Alaska	NASD
Deutsche Bank*	California	Maryland and District of Columbia	SEC
UBS Paine Webber	Arizona, Illinois	Connecticut, Nevada, Oklahoma	NYSE

*Settlement in Principle

	State	Population	% US Pop	Bear Stearns Settlement	CSFB Settlement	Deutsche Bank Settlement	Goldman Sachs Settlement	JP Morgan Settlement	Lehman Brothers Settlement	Morgan Stanley Settlement	Salomon Smith Barney Settlement	UBS Warburg Settlement	Piper Jaffray Settlement	TOTAL SETTLEMENT
1	California	33,871,648	11.88%	2,609,851	7,829,548	2,609,851	2,609,851	2,609,851	2,609,851	2,609,851	15,659,096	2,609,851	1,304,926	43,062,527
2	Texas	20,851,820	7.31%	1,606,657	4,819,970	1,606,657	1,606,657	1,606,657	1,606,657	1,606,657	9,639,939	1,606,657	803,329	26,509,837
3	New York	18,976,457	6.65%	1,462,158	4,386,473	1,462,158	1,462,158	1,462,158	1,462,158	1,462,158	8,772,946	1,462,158	731,079	24,125,604
4	Florida	15,982,378	5.60%	1,231,461	3,694,382	1,231,461	1,231,461	1,231,461	1,231,461	1,231,461	7,388,763	1,231,461	615,731	20,319,103
5	Illinois	12,419,293	4.35%	956,921	2,870,762	956,921	956,921	956,921	956,921	956,921	5,741,524	956,921	478,461	15,789,194
6	Pennsylvania	12,281,054	4.31%	946,269	2,838,808	946,269	946,269	946,269	946,269	946,269	5,677,615	946,269	473,135	15,613,441
7	Ohio	11,353,140	3.98%	874,773	2,624,317	874,773	874,773	874,773	874,773	874,773	5,248,634	874,773	437,386	14,433,748
8	Michigan	9,938,444	3.48%	765,768	2,297,305	765,768	765,768	765,768	765,768	765,768	4,594,611	765,768	382,884	12,635,176
9	New Jersey	8,414,350	2.95%	648,335	1,945,006	648,335	648,335	648,335	648,335	648,335	3,890,011	648,335	324,168	10,697,530
10	Georgia	8,186,453	2.87%	630,775	1,892,326	630,775	630,775	630,775	630,775	630,775	3,784,653	630,775	315,388	10,407,792
11	North Carolina	8,049,313	2.82%	620,209	1,860,626	620,209	620,209	620,209	620,209	620,209	3,721,252	620,209	310,104	10,233,445
12	Virginia	7,078,515	2.48%	545,408	1,636,223	545,408	545,408	545,408	545,408	545,408	3,272,446	545,408	272,704	8,999,229
13	Massachusetts	6,349,097	2.23%	489,205	1,467,615	489,205	489,205	489,205	489,205	489,205	2,935,231	489,205	244,602	8,071,883
14	Indiana	6,080,485	2.13%	468,508	1,405,525	468,508	468,508	468,508	468,508	468,508	2,811,050	468,508	234,254	7,730,385
15	Washington	5,894,121	2.07%	454,149	1,362,446	454,149	454,149	454,149	454,149	454,149	2,724,892	454,149	227,074	7,493,455
16	Tennessee	5,689,283	1.99%	438,366	1,315,097	438,366	438,366	438,366	438,366	438,366	2,630,194	438,366	219,183	7,233,036
17	Missouri	5,595,211	1.96%	431,117	1,293,352	431,117	431,117	431,117	431,117	431,117	2,586,704	431,117	215,558	7,113,433
18	Wisconsin	5,363,675	1.88%	413,277	1,239,832	413,277	413,277	413,277	413,277	413,277	2,479,663	413,277	206,638	6,819,072
19	Maryland	5,296,486	1.86%	408,100	1,224,301	408,100	408,100	408,100	408,100	408,100	2,448,601	408,100	204,050	6,733,652
20	Arizona	5,130,632	1.80%	395,321	1,185,963	395,321	395,321	395,321	395,321	395,321	2,371,926	395,321	197,660	6,522,796
21	Minnesota	4,919,479	1.72%	379,051	1,137,154	379,051	379,051	379,051	379,051	379,051	2,274,309	379,051	189,526	6,254,346
22	Louisiana	4,468,976	1.57%	344,339	1,033,019	344,339	344,339	344,339	344,339	344,339	2,066,038	344,339	172,170	5,681,600
23	Alabama	4,447,100	1.56%	342,654	1,027,962	342,654	342,654	342,654	342,654	342,654	2,055,924	342,654	171,327	5,653,791
24	Colorado	4,301,261	1.51%	331,417	994,251	331,417	331,417	331,417	331,417	331,417	1,988,502	331,417	165,708	5,468,380
25	Kentucky	4,041,769	1.42%	311,423	934,268	311,423	311,423	311,423	311,423	311,423	1,868,537	311,423	155,711	5,138,477
26	South Carolina	4,012,012	1.41%	309,130	927,390	309,130	309,130	309,130	309,130	309,130	1,854,780	309,130	154,565	5,100,645
27	Puerto Rico	3,808,610	1.34%	293,457	880,373	293,457	293,457	293,457	293,457	293,457	1,760,746	293,457	146,729	4,842,047
28	Oklahoma	3,450,654	1.21%	265,877	797,630	265,877	265,877	265,877	265,877	265,877	1,595,261	265,877	132,938	4,386,968
29	Oregon	3,421,399	1.20%	263,622	790,868	263,622	263,622	263,622	263,622	263,622	1,581,736	263,622	131,811	4,349,769
30	Connecticut	3,405,565	1.19%	262,402	787,208	262,402	262,402	262,402	262,402	262,402	1,574,416	262,402	131,201	4,329,639
31	Iowa	2,926,324	1.03%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
32	Mississippi	2,844,658	1.00%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
33	Kansas	2,688,418	0.94%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
34	Arkansas	2,673,400	0.94%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
35	Utah	2,233,169	0.78%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
36	Nevada	1,998,257	0.70%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
37	New Mexico	1,819,046	0.64%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
38	West Virginia	1,808,344	0.63%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
39	Nebraska	1,711,263	0.60%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
40	Idaho	1,293,953	0.45%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
41	Maine	1,274,923	0.45%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
42	New Hampshire	1,235,786	0.43%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
43	Hawaii	1,211,537	0.42%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
44	Rhode Island	1,048,319	0.37%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
45	Montana	902,195	0.32%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
46	Delaware	783,600	0.27%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
47	South Dakota	754,844	0.26%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
48	North Dakota	642,200	0.23%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
49	Alaska	626,932	0.22%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
50	Vermont	608,827	0.21%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
51	District of Columl	572,059	0.20%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
52	Wyoming	493,782	0.17%	250,000	750,000	250,000	250,000	250,000	250,000	250,000	1,500,000	250,000	125,000	4,125,000
	State Total	285,230,516		25,000,000	75,000,000	25,000,000	25,000,000	25,000,000	25,000,000	25,000,000	150,000,000	25,000,000	12,500,000	412,500,000
	Total Settlement			50,000,000	150,000,000	50,000,000	50,000,000	50,000,000	50,000,000	50,000,000	300,000,000	50,000,000	25,000,000	825,000,000
	State Settlement			**25,000,000**	**75,000,000**	**25,000,000**	**25,000,000**	**25,000,000**	**25,000,000**	**25,000,000**	**150,000,000**	**25,000,000**	**12,500,000**	412,500,000
	Minimum			**250,000**	**750,000**	**250,000**	**250,000**	**250,000**	**250,000**	**250,000**	**1,500,000**	**250,000**	**125,000**	4,125,000
	Maximum			25,000,000	75,000,000	25,000,000	25,000,000	25,000,000	25,000,000	25,000,000	150,000,000	25,000,000	12,500,000	412,500,000
	Max/Min Adj Factor			0.8790940995	0.8790936300	0.8790940995	0.8790940995	0.8790940995	0.8790940995	0.8790940995	0.8790935400	0.8790940995	0.8790947000	

Payments in Global Settlement Relating to
Firm Research and Investment Banking Conflicts of Interest

Firm	Penalty ($ millions)	Disgorgement ($ millions)	Independent Research ($ millions)	Investor Education ($ millions)	Total ($ millions)
Bear Stearns	25	25	25	5	**80**
CSFB	75	75	50	0	**200**
Goldman	25	25	50	10	**110**
J.P. Morgan	25	25	25	5	**80**
Lehman	25	25	25	5	**80**
Merrill Lynch	100*	0	75	**	**200**
Morgan Stanley	25	25	75	0	**125**
Piper Jaffray	12.5	12.5	7.5	0	**32.5**
SSB	150	150	75	25	**400**
UBS Warburg	25	25	25	5	**80**
Total ($ millions)	**487.5**	**387.5**	**432.5**	**55**	**$1,387.5**

*Payment made in prior settlement of research analyst conflicts of interest with state securities regulators.
**Payment of $25 million to Federal investor education fund only.

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NEWS AND PUBLIC AFFAIRS
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"Top 10" Investment Scams Listed by State Securities Regulators

WASHINGTON (August 26, 2002) – State securities regulators today released a list of the "Top 10" scams, risky investments or sales practice abuses they're fighting. New to the third annual list are unscrupulous brokers, conflicts of interest in analyst research, charitable gift annuities, and oil and natural gas scams.

"Record-low interest rates and a bear market on Wall Street have created a bull market in fraud on Main Street," said Joseph Borg, president of the North American Securities Administrators Association (NASAA)[1] and director of the Alabama Securities Commission. "Con artists know investors are concerned about the volatile stock market and low yields on bonds and bank deposits, so they pitch their scams as safe alternatives and promise high returns – an impossible combination."

The 2002 list was again topped by independent insurance agents selling risky or fraudulent securities. Borg said that while most independent insurance agents are honest professionals, too many are letting high commissions lure them into selling high risk or fraudulent investments.

The federal war on terror and large budget deficits at the state level are diverting or pinching resources to fight investment fraud, Borg warned.

"Putting people in jail gives investors the biggest bang for their regulatory buck," said Borg. "So legislators at all levels need to ensure that regulators and prosecutors have sufficient resources to successfully bring securities fraud cases."

Here are the "Top 10" investment scams, ranked roughly in order of prevalence or seriousness:

1. Unlicensed individuals, such as independent insurance agents, selling securities. In hundreds of cases from Washington state to Florida, scam artists are using high commissions to entice independent insurance agents into selling investments they may know little about. The person running the scam instructs the independent sales force – usually insurance agents but sometimes investment advisers and accountants – to promise high returns with little or no risk. For example:
· In an alleged scam sold almost entirely by independent insurance agents, investors in at least 14 states lost close to $30 million. According to Ohio securities regulators, money raised from the sale of fictitious limited partnerships was used to make interest payments to another group of promissory note investors. Both groups were promised double-digit returns. In April a court issued a preliminary injunction and appointed a receiver in connection with the allegations.

· Earlier this month, an Arizona insurance agent was sentenced to 10 years in prison for selling $1.8 million in worthless stock and bogus promissory notes to investors. Another Arizona insurance agent was sentenced in May to five years in prison for scamming 32 elderly investors out of nearly $2 million by first soliciting them to purchase 'living trusts' and then switching them into annuities and finally into bogus promissory notes. A third Arizona insurance agent, working with his two sons, scammed $16.2 million by selling high risk brokered CDs, viatical contracts, real estate deals and equipment leases. They were ordered to repay all $16.2 million and fined another $133,000.

To verify that a person is licensed or registered to sell securities, call your state securities regulator. If the person is not registered, don't invest.

2. **Unscrupulous stockbrokers.** The declining stock market has caused some brokers to cut corners or resort to outright fraud, say state securities regulators. At the same time, some investors have grown more cautious and are scrutinizing their brokerage statements for unexplained fees, unauthorized trades or other irregularities. In North Dakota, regulators investigated a complaint from an investor who received conflicting account statements. They discovered that two brokers working for H.D. Vest Investment Securities Inc. issued phony account statements to cover up losses from hundreds of unauthorized trades. The brokers had also made unsuitable recommendations such as risky options contracts. Under a settlement with state securities regulators, H.D. Vest agreed to repay clients' out-of-pocket losses plus 6 percent, totaling over $3.2 million.

In New York, the attorney general's office took action against seven brokers and two firms for bilking hundreds of elderly investors out of more than $12.5 million through a pay telephone scam. The brokers pressured investors into liquidating their CDs, annuities and IRAs, sometimes at significant penalty, and promised them "risk-free" 14 percent returns. So far one firm has agreed to pay $5.9 million in restitution.

3. **Analyst research conflicts.** In May, the New York Attorney General's office concluded a 10-month investigation into whether Merrill Lynch had issued misleading research reports by entering into a settlement agreement with the firm. Under the agreement, Merrill Lynch agreed to pay a $100 million fine and make significant changes to way it does business. NASAA is assisting a multi-state task force investigating conflict of interest issues at Wall Street firms. The primary focus of the ongoing investigation is to determine whether analysts issued glowing research reports and made "buy" recommendations in order to win investment-banking business. State investigators are now reviewing materials provided by a dozen firms for possible securities law violations.

In June NASAA learned of an attempt by Morgan Stanley Dean Witter to amend an early version of the Sarbanes-Oxley Act with language that would have ended the states' probe into whether Wall Street analysts intentionally misled investors. NASAA held a press conference and met with lawmakers; the draft amendment was ultimately not included in the bill.

4. **Promissory notes.** These are short-term debt instruments often sold by independent insurance agents and issued by little known or non-existent companies promising high returns – upwards of 15 percent monthly – with little or no risk.

In June, four Georgia-based scam artists were each sentenced to 17 ½ years in prison for recruiting independent insurance agents to sell millions of dollars worth of bogus promissory notes. While investors were promised nine-month returns as high as 21 percent, half of each investment went straight to commissions that were divided among company principals and sales agents. Acting on a tip from the Better Business Bureau, Georgia securities regulators seized nearly $5 million of the $8 million stolen from local investors and, together with federal investigators, used the evidence uncovered to broaden their investigation and prepare criminal charges. In the end, the Federal Bureau of Investigation, working with Georgia regulators, found the ringleader – Virgil Womack – had scammed over $150 million from investors nationwide. Of the $150 million, nearly $90 million was seized and returned to investors. The average age of the victims was 68.

In another case, a Maine court sentenced an insurance agent to seven years in prison for running a promissory note scam that took 25 investors for more than $1 million. The agent, who was sentenced in June, told investors the notes were "better than certificates of deposit and life insurance policies," regulators said, and that they would yield 10 percent to 12 percent returns annually.

"A 12 percent return may not seem over-the-top by bull market standards, but it's far more than banks are offering now for insured deposits," said Chris Bruenn, administrator for the Maine Office of Securities and NASAA's president-elect.

5. **"Prime bank" schemes.** Scammers promise investors triple-digit returns through access to the investment portfolios of the world's elite banks. Purveyors of these schemes often target conspiracy theorists, promising access to the

"secret" investments used by the Rothschilds or Saudi royalty.

In Texas, a Harlingen-based con artist promised returns of 6 percent to 8 percent a month through a secretive web of money dealers supposedly set up by a coalition of governments in 1914 to pay for World War I debt. In videotape shown at Monday's press conference, the promoter claimed that seven "world traders" control the entire global money supply. In the end, the scam took over 300 investors for roughly $6 million.

6. **Viatical settlements.** Originated as a way to help the gravely ill pay their bills, these interests in the death benefits of terminally ill patients are always risky and sometimes fraudulent. The insured gets a percentage of the death benefit in cash and investors get a share of the death benefit when the insured dies. Because of uncertainties predicting when someone will die, these investments are extremely speculative. In a new twist, Pennsylvania regulators say "senior settlements" – interests in the death benefits of healthy older people – are now being offered to investors.

In June, 15 individuals were indicted in connection with a scam that cost hundreds of investors nationwide at least $100 million. State securities and insurance regulators, together with federal regulators, allege the individuals, employed by Liberte Capital Group, were involved in a scheme to buy life insurance policies from terminally ill individuals who lied to insurance companies about their medical conditions. Liberte managers used investor funds to support lavish lifestyles, including investments and the purchase of large homes and dozens of boats and cars. A receiver has been appointed in the case.

7. **Affinity fraud.** Many scammers use their victim's religious or ethnic identity to gain their trust – knowing that it's human nature to trust people who are like you – and then steal their life savings. From "gifting" programs at some churches to foreign exchange scams targeted at Asian Americans, no group seems to be without con artists who seek to take advantage of the trust of others.

In Alabama, nine individuals have been charged with scamming parishioners at the Daystar Assembly of God church in Prattville out of more than $3 million. Investors were told their money would be used to purchase retirement properties in Florida. The income generated by the Florida properties would be used to payoff the mortgage of the Prattville church and build a religious theme park, investors were told. In reality, state securities regulators allege, the money went to pay off investors in a previous scam and to purchase equipment for unrelated businesses.

8. **Charitable gift annuities.** These annuities are transfers of cash or property to a charitable organization. The value of the annuity is less than the value of the cash or property, with the difference constituting a charitable donation. While most annuities offered by charitable organizations are legitimate investments, investors should be cautious of little-known organizations or those that provide only sketchy information.

In Arizona, regulators uncovered a scam that took 430 investors nationwide for an average of $133,000. The scam involved the purchase of charitable gift annuities from the Mid-America Foundation. According to regulators, Robert Dillie, founder of Mid-America, ran what amounted to a $54 million Ponzi scheme through a network of independent insurance agents, financial planners and accountants. Dillie used investors' funds to purchase three homes in Las Vegas, a ranch in South Dakota, pay child support, book charter flights and support his extensive gambling.

Magdalena Scheller, 68, of Phoenix, invested more than $400,000 in Mid-America. A life insurance agent approached her after her husband died.

"It makes you wonder if there are any honest people out there," Scheller said at Monday's press conference.

"Unfortunately, Mid-America is not an isolated scam," Mark Sendrow, director of securities for the Arizona Corporation Commission told reporters Monday. "We are looking at two more foundations in the Phoenix area which have issued millions of dollars of charitable gift annuities in the last few years, and both were basically penniless before they began issuing them."

9. **Oil and gas schemes.** These scams follow the headlines, rising in frequency with predictions of oil shortages or a rise in natural gas prices. In Arkansas, securities regulators forced Energy Consultants and Ark-La-Tex Consulting Co.,

L.L.C. to discontinue their marketing efforts after finding a natural gas well touted to investors as a 'can't lose' opportunity hadn't produced in years.

10. **Equipment leasing.** While the majority of equipment leasing deals are legitimate, thousands of investors have been scammed by individuals selling interests in payphones, ATMs or Internet kiosks. In a typical equipment leasing scam, a company sells a piece of equipment through a middleman. As part of the sale, the company agrees to lease back and service the equipment for a fee. Investors are promised high returns with little or no risk. But state regulators say high commissions paid to salesmen and promised returns that are unrealistically high doom many projects. In North Carolina, regulators took action against an individual who sold an Internet kiosk to an investor for $24,950, promising a 17 percent return. The individual had previously sold payphone leases to investors from a company that later filed for bankruptcy.

Before investing, state securities regulators urge investors to call their offices and ask if the individual selling the investment is licensed to do so. Regulators say investors can also save themselves a lot of grief by asking a second question – whether the investment itself is registered. To check out an investment or salesperson, contact your state securities regulator. Their phone number is in the white pages of your phone book under "government" or available online at www.nasaa.org.

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[1] NASAA, the oldest international organization devoted to investor protection, was organized in 1919. It is a voluntary association with a membership consisting of the 66 state, provincial and territorial securities administrators in the 50 states, the District of Columbia, Canada, Mexico and Puerto Rico. In the U.S., NASAA is the national voice of the 50 state securities agencies responsible for investor protection and the efficient functioning of the capital markets at the grassroots level.

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